

BUSINESS STRUCTURE AND NAME REGISTRATION

Establishing a business in the state of Arizona is a simple process. The first step is to determine which form of business structure is most appropriate for your operations. To do this, an analysis of the various legal and tax-related implications associated with the forms of business structure must be conducted. In Arizona, as in all states, several business structures exist. The four most common are the sole proprietorship, general and limited partnerships, limited liability company, and corporation. The state also recognizes a limited liability partnership.

The following section provides a brief description of each, including general advantages and disadvantages. An attorney and/or certified public accountant should be consulted for further information and advice on selecting the appropriate structure for your business. Once you have determined the legal structure of your business, the next step is to complete the necessary registration requirements. Most businesses are required to register with the state and/or county in which the enterprise will operate, and these registration requirements vary.

Sole Proprietorship

The sole proprietorship is the simplest and most common form of business organization. A sole proprietorship is defined as a business that is owned by one individual. The owner is personally responsible for all debts of the firm. Profits are considered as personal income and taxed accordingly.

Advantages of a sole proprietorship include:

- Minimum legal restrictions
- Ease of formation
- Low start-up costs
- Sole ownership of profits
- Maximum freedom in decision-making

Disadvantages of a sole proprietorship include:

- Unlimited liability
- Less available capital than in other types of business organizations
- Relative difficulty in obtaining long-term financing

If the business is going to be a sole proprietorship operating under a name other than your own, you should register the business name (commonly known as "doing business as" or "DBA") with the Arizona Secretary of State's Trademark and Trade Name registration office and the County Recorder of the county in which you will operate.

The Secretary of State's office is located at 1700 West Washington Street, 7th Floor, Phoenix, Arizona 85007. The telephone number is (602) 542-6187 or statewide toll free (800) 458-5842.

General Partnership

A general partnership is an association of two or more persons joined together to carry on trade or business for profit. As in the sole proprietorship, partners are personally responsible for all debts of the firm. The partnership's existence is usually formalized through preparation of a partnership agreement. Formal partnership agreements should be prepared by, or at least reviewed by, an attorney. In general, partnership agreements outline each partner's share of income, gain, loss, deductions, credits, and methods to dissolve the partnership under various situations including death of one or more partners.

Advantages of a partnership include:

- Ease of formation
- Direct rewards
- Broader management base

Disadvantages of a partnership include:

- Unlimited liability of general partners
- Divided authority in decision-making
- Difficulty in disposing of partnership interest

General partnerships transacting business in Arizona under a fictitious name, or a designation not showing the names of the partners, should register the business name "doing business as" or "DBA" with the Arizona Secretary of State's Trademark and Trade Name registration office and the County Recorder of the county in which the business is located.

The Secretary of State's office is located at 1700 West Washington Street, 7th Floor, Phoenix, Arizona 85007. The telephone number is (602) 542-6187 or statewide toll free (800) 458-5842.

Limited Partnership

This form is similar to the general partnership with several major differences.

Some of these differences include:

- At least one person must be identified as a general partner and be responsible for the operation and liability of the organization
- Limited partners are not active managers of the business and are not liable for the organization's debts, etc.

If the business is a limited partnership, domestic (Arizona-based) or foreign (not Arizona-based), you are required to register with the Arizona Secretary of State's Trademark and Trade Name registration office, 1700 West Washington Street, 7th Floor, Phoenix, Arizona 85007; telephone (602) 542-6187 or statewide toll free (800) 458-5842. The business name should also be registered with the County Recorder of the county in which the business is located.

Limited Liability Partnership

Limited Liability Partnership (LLP) is a recent form of business entity in Arizona. For additional information regarding an LLP, please contact an attorney or your county bar association. The lack of clear legal precedent could be a disadvantage.

To register a Limited Liability Partnership, domestic or foreign, please contact the Arizona Secretary of State's office, 1700 West Washington Street, 7th Floor, Phoenix, AZ 85007. The telephone number is (602) 542-6187 or statewide toll free (800) 458-5842.

Corporation

A corporation, sometimes referred to as a "C Corporation," is the most complex type of business organization. It is formed by law as a separate entity, completely distinct from those who own it, and has its own rights and responsibilities.

In forming a corporation, potential shareholders offer money and/or property in exchange for capital stock. The stockholders are the owners of the corporation and the managers of the firm may or may not be stockholders. Businesses that incorporate in this state must file Articles of Incorporation with the Arizona Corporation Commission.

Out-of-state corporations wishing to do business in the state must file an Application for Authority to Transact Business.

Advantages of a corporation include:

- Separate legal entity
- Limited liability for stockholders
- Unlimited life for the business
- Relative ease in raising capital
- Transfer of ownership through sale of stock
- Ability to draw on the skills and expertise of more than one individual

Disadvantages of a corporation include:

- Complex and relatively expensive to organize
- Activities limited by the corporate charter
- Extensive regulation and record-keeping requirements
- Double taxation - once on corporate profits and again on dividends

Incorporation of a business in Arizona involves the following steps:

1. Make sure that the name you plan to use has been checked with the Arizona Corporation Commission and is available for use by your corporation. A business name may be reserved for 120 days.
2. Deliver the original and one or more copies of the Articles of Incorporation to the Corporation Commission.
3. Show a street address for the statutory agent (P.O. Box not accepted).
4. File Certificate of Disclosure (included in the incorporation application forms).
5. Pay the required fees.
6. Advise the commission, in writing, of the fiscal year to be used by the corporation.
7. Publish the Articles of Incorporation within 60 days after filing with the Arizona Corporation Commission. The Articles must be published in three consecutive issues of a newspaper in general circulation in the Arizona county of the corporation's known place of business. Within 90 days after filing, an affidavit of this publication must also be filed with the Arizona Corporation Commission.

Foreign Corporation

If the business is a foreign corporation (an entity organized under the laws of another state or country), it must be registered with the Arizona Corporation Commission.

Foreign corporations applying for Authority to Transact Business in Arizona must comply with the following at the time of filing:

1. Make sure the name that you are using has been checked with the Arizona Corporation Commission and is available for use by your corporation. The name may be reserved for 120 days.
2. Deliver the original and one or more copies of the Application for Authority to the Corporation Commission.
3. Show a street address for the statutory agent (P.O. Box not accepted).
4. File Certificate of Disclosure (included in application forms).
5. Pay the required fees.
6. Advise the Corporation Commission, in writing, of the fiscal year to be used by the corporation.
7. Publish the Application for Authority within 60 days after filing with the Arizona Corporation Commission. The application must be published in three consecutive issues of a newspaper in general circulation in the Arizona county of the corporation's known place of business. Within 90 days after filing, an affidavit of this publication must also be filed with the Arizona Corporation Commission.

Additional information on incorporating may be obtained from the Arizona Corporation Commission, Corporations Division, 1300 West Washington Street, Phoenix, Arizona 85007, (602) 542-3135; or 400 West Congress Street, Suite 221, Tucson, Arizona 85701, (520) 628-6560 or statewide toll free (800) 345-5819.

S Corporation

Subchapter S Corporations, also referred to as "S Corporations," elect not to be subject to federal corporate income tax. The shareholders, however, include their shares of the corporation's items of income, deduction, loss, and credit, or their shares of non-separately computed income or loss, as part of their personal income.

To qualify for S Corporation status, a corporation must meet the following requirements:

- It must be headquartered in the United States
- It must have only one class of stock
- It must have no more than 35 shareholders
- One individual may serve as both President and Secretary
- It cannot have any Non-Resident Alien as a shareholder

Until 1997, certain restrictions had existed on the ownership of Subchapter S Corporations by corporations, trusts and pension plans. Recent changes in the tax laws have liberalized these rules; however, current restrictions must be checked carefully at the time of filing. Please refer to your attorney and Certified Public Accountant for further information regarding the changes in law. Publications may contain outdated information.

A corporation meeting all of the above criteria can become an S Corporation if:

1. All shareholders consent to the corporation's election of S Corporation status.
2. The corporation has a permitted tax year.
3. IRS Form 2553, Election by a Small Business Corporation, is filed to indicate the choice of S Corporation status. The corporation must qualify as an S Corporation at the time it files Form 2553.

For more information on S Corporations, obtain IRS Publication 589, Tax Information on S Corporations, from the IRS Forms Distribution Center, Rancho Cordova, California 95743-0001. The telephone number is (800) 829-3676.

To incorporate your business, contact the Arizona Corporation Commission, 1300 West Washington Street, Phoenix, Arizona 85007, (602) 542-3230; or 400 West Congress Street, Suite 221, Tucson, Arizona 85701, (520) 628-6560.

Limited Liability Company (LLC)

A Limited Liability Company offers businesses the protection of a corporation and the single taxation feature of a partnership.

Limited Liability Company Advantages:

- Limited disclosure of owners
- Limited documentation (organization and annual)
- No advance IRS filings (as with S Corporation)
- No public disclosure of finances
- Lower filing fees
- Professional LLC's are allowed
- Can build in buy/sell and owner compensation provision - no separate document
- Ease in transfer of ownership
- Can use special allocations between owners
- Can use different classes of owners
- Member (owner) involved in LLC operation insulated from liability
- Can assign management to a non-member

Limited Liability Company Disadvantages:

- Out-of-state business complicates status if the other state does not recognize LLC
- Large number of owners complicates status
- Death, bankruptcy, or withdrawal of owner could cause problems

Tax Provisions Advantages:

- No tax at LLC level
- Established and well-seasoned partnership rules apply
- No new Federal ID number required when converting from partnership to LLC
- No withholding tax on owners' salaries
- No double tax on appreciation ("built-in gain")
- More flexible restructuring possible
- No problem with retained earnings
- Easier structuring of debt
- Step-up in tax basis on death of member or sale of interest
- Less tax on owners' retirement pay
- Tax-free distribution of assets possible
- Flexibility in contribution of assets to the LLC
- Member's "outside" expenses not classified as miscellaneous itemized deduction subject to 2 percent disallowance

Tax Provisions Disadvantages:

- Status of self-employed tax on owners uncertain
- Status of sales tax on owners/lessees uncertain
- Some gain on appreciation may be taxed as ordinary income
- No shifting of appreciation on contribution of property to LLC

To register a Limited Liability Company, domestic or foreign, please contact the Arizona Corporation Commission, 1300 West Washington Street, Phoenix, Arizona 85007, (602) 542-3135; or 400 West Congress Street, Suite 221, Tucson, Arizona 85701, (520) 628-6560 or statewide toll free (800) 345-5819.

The Department of Commerce acknowledges Ira S. Feldman, CPA, of Toback CPAs P.C., for providing information on the Limited Liability Company.

Tax-Exempt Organizations (Non-Profit Corporations)

There are over a dozen different types of corporations approved by the Internal Revenue Service as "Non-Profits." These organizations are usually developed and operated exclusively for one or more of the following purposes: charitable, religious, educational, scientific, literary, testing for public safety, fostering amateur sports competition (under certain restrictions), or the prevention of cruelty to children or animals. The organization must be a corporation, community chest fund or foundation. A sole proprietorship or partnership will not qualify.

Other organizations that may qualify include: civic leagues, social welfare organizations, labor, agriculture and horticultural organizations, business leagues, social and recreation clubs, fraternal beneficiary societies, etc.

For a free IRS booklet on this subject, call (800) 829-3676 and request publication 557.

To register a Non-Profit Corporation, contact the Arizona Corporation Commission, 1300 West Washington Street, Phoenix, Arizona 85007, (602) 542-3135; or 400 West Congress Street, Suite 221, Tucson, Arizona 85701, (520) 628-6560 or statewide toll free (800) 345-5819.